



Appeal of General Telephone Company of California

The principal issue is whether appellant could unilaterally apply as a credit against its self-assessed tax liability for the income year 1973 the amount of a refund claim for an earlier year which had not been acted upon by respondent.

On June 7, 1973, the Internal Revenue Service adopted Treasury Regulation 1.167(a)-12 which prescribes a different set of "guidelines" or depreciable lives for certain assets placed in service prior to January 1, 1971. It thereby **increased** allowable depreciation expenses. The regulation applied retroactively to the year 1971. Thus, appellant, a California corporation, filed an amended 1971 federal income tax return as part of an amended consolidated return filed by General Telephone and Electronics Corporation (GTE) and its subsidiaries.

On September 13, 1973, appellant and Western California Telephone Company (Western), also an affiliate of GTE, filed an amended California franchise tax return for the income year 1971, reflecting their adoption of these guidelines. In the amended state return, appellant claimed it overpaid California franchise tax for the income year 1971 in the amount of **\$1,475,185**, and directed that the overpayment be applied against appellant's 1972 estimated tax. Western claimed it overpaid franchise **tax in** the amount of \$33,023.

On September 14, 1973, appellant filed its franchise tax return for the income year 1972, using the new method of computing depreciation and claiming the alleged overpayment of tax for 1971 in the amount of **\$1,475,185** as a credit against its tax liability for the income year 1972. Appellant's total payments for that year, when added to the claimed credit, exceeded its tax liability for 1972 by **\$2,915,619**. On its 1972 return, appellant elected to carry that amount forward as a credit on its 1973 estimated tax.

On January 21, 1974, respondent notified appellant that its resulting refund claim for the income year 1972 was granted to the extent of **\$1,440,434** (plus applicable interest), but in computing the amount of refund due the asserted overpayment of **\$1,475,185** was not considered. It was explained that **action** on the claim for refund for the income year 1971 would only be taken upon completion of a pending audit.

This reference was to a complex audit involving appellant's parent and its subsidiaries. The principal

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questions involved in that audit are whether some or all of the corporations are part of a unitary business,, and the proper treatment of intercorporate dividends. The 1971 refund claim remains unresolved pending completion of the audit.

On September 11, 1974, appellant filed its franchise tax return for the income year 1973, and offset against self-assessed tax liability the total payments previously made for that year and the credit authorized by respondent by its notification of January 21, 1974. Despite respondent's previous explanation concerning the unavailability of such a credit, appellant also attempted to credit the alleged \$1,475,185 overpayment of tax for the year 1971. By including the last credit, the return reflected an overpayment of \$152,547 for the income year 1973, which appellant requested be applied to 1974 estimated tax.

On January 17, 1975, respondent again notified appellant of its refusal to allow the latter credit because respondent had not taken any final action on the refund claim for the income year 1971. Accordingly, respondent determined that self-assessed tax in the amount of \$1,315,435.83 for the income year 1973 remained unpaid. It then also indicated that appellant was liable for a \$1,000 penalty for that underpayment of tax, pursuant to the provisions of section 25934.2. The penalty has not been paid.

Appellant alleges that it is entitled to the \$1,475,185 credit because of the following circumstances: (1) Respondent allowed appellant's refund claim for the income year 1972 based on use of the new depreciation method in 1972, and (2) Western's refund claim for the income year 1971 was allowed, and the activities of Western, as a subsidiary of GTE, are also included in the same complex audit. In view of these factors it is urged that respondent is not seriously contesting appellant's refund claim for the income year 1971, and that the revised depreciation method is not a subject of dispute in the audit. Therefore, the fact that the audit is not completed because of undue delays does not constitute, in appellant's view, a legitimate basis for disallowing the credit.

Appellant also maintains that respondent's refusal to allow the credit violates the equal protection clause of the 14th amendment to the federal Constitution. Relying upon the distinction in respondent's method of

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-treating the 1971 refund claims of appellant and Western, appellant alleges invidious discrimination. It claims that, in applying the same statute and regulation, there is no rational basis for discriminating between two members of the same class when the factual situation applicable to each is identical.

The pertinent statutory provision is section 26072. It provides that if respondent determines a taxpayer has overpaid the tax, respondent shall set forth that fact in its records and may either credit the amount on any amounts then due and payable, or refund the amount or the balance to the taxpayer. It also provides that no refund exceeding \$10,000 is to be allowed or made until approved by the State Board of Control.

The applicable regulation specifically provides that a taxpayer may not on its own initiative offset an overpayment for one year against taxes due for another year: the full amount of the tax for each year must be paid, notwithstanding that overpayment may have been made, unless the taxpayer has filed a claim for refund of the overpayment and has been notified that the overpayment has been credited. (Cal. Admin. Code, tit. 18, reg. 26071-26080.3, subd. (g).)

This regulation requires the conclusion that **respondent must determine an overpayment** of tax has been made, and the State Board of Control must approve (where the amount exceeds \$10,000), before the amount of the overpayment may be credited by a taxpayer. This regulation is consistent with the code provision. It is merely a statement that the unilateral action of a taxpayer in taking the credit is not the equivalent of the required procedure. (Appeal of George French, Jr. and Mary E. French, Cal. St. Bd. of Equal., Dec. 16, 1958.) TO permit taxpayers to offset alleged but unproved overpayments against their current tax liabilities would create chaos in the collection of taxes. (See Appeal of George French, Jr. and Mary E. French, supra.)

Consequently, appellant's total tax liability for the income year 1973 could not be considered as paid because the claimed credit was not validly established. Appellant's attempted application of an invalid credit left it deficient in payment of self-assessed tax for that income year in the amount of \$1,315,435.83.

With respect to appellant's objections to the penalty, inasmuch as it has not been paid we must conclude that this board lacks jurisdiction concerning this matter.

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Finally, in reference to appellant's constitutional arguments, there appears to be an absence of any invidious discrimination resulting in denial of equal protection. In view of the audit in process, respondent was presumably exercising its statutory responsibility in attempting to determine the correct tax liability for the year 1971. If it is ultimately determined that appellant had actually underpaid its tax for 1971 because of other adjustments, there would be no overpayment to be refunded or credited. (See United States v. Memphis Cotton Oil Co., 288 U.S. 62 [77 L. Ed. 6191 (1933).]) Furthermore, the granting of Western's 1971 claim for refund may have inadvertently occurred. A discriminatory intent is not presumed: an element of intentional or purposeful discrimination must be shown. (City of Banning v. Desert Outdoor Advertising, Inc., 209 Cal. App. 2d 152 [25 Cal. Rptr. 6211 (1962).])

Accordingly, respondent's action must be sustained.

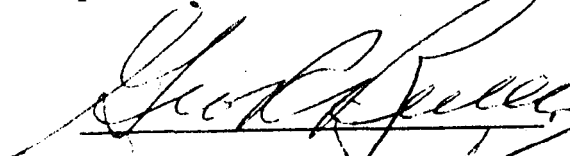


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O R D E R

Pursuant to the views expressed in the opinion of the board on file in this proceeding, and good cause appearing **therefor**,

IT IS HEREBY ORDERED, ADJUDGED AND DECREED, pursuant to section 26077 of the Revenue and Taxation Code, that the action of the Franchise Tax Board in denying the claim of General Telephone Company of California for refund of franchise tax in the amount of \$152,547 for the income year 1973, be and the same is hereby sustained. It is further ordered that the appeal concerning the penalty in the amount of \$1,000 for the income-year 1973, be and the same is hereby dismissed.

Done at Sacramento, California, this 27th day of September, 1978, by the State Board of Equalization.


_____, Chairman

_____, Member

_____, Member
_____, Member
_____, Member